No. 16,106

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

vs.

HERBERT D. HOVER, Doing Business as Ciro's,

Appellee.

On Appeal From the Judgment of the United States District Court for the Southern District of California.

BRIEF FOR THE APPELLEE.

ERNEST R. MORTENSON,
961 East Green Street,
Pasadena, California,
Attorney for Appellee.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

TOPICAL INDEX

TABLE OF AUTHORITIES CITED

Cases

Regulations and Rules

No. 16,106

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

vs.

HERBERT D. HOVER, Doing Business as Ciro's,

Appellee.

On Appeal From the Judgment of the United States District Court for the Southern District of California.

BRIEF FOR THE APPELLEE.

Jurisdiction.

The District Court had jurisdiction of this matter under 28 U. S. C. A., Sec. 1346. This Court has jurisdiction under 28 U. S. C., Sec. 1291.

Statutes Involved.

Appellant has set out the pertinent statutes and regulations in Appendix "A" to its opening brief.

Statement.

Appellant has given us most of the pertinent facts in its opening brief; however, it might be helpful to the Court to restate a few of the facts. The Government assessed cabaret taxes against appellee in the amount of

$67,660.62. Because of a clerical error, appellee has underpaid his cabaret taxes by $992.00, which amount is not in dispute. By stipulation it was agreed that $5,200.63 represented the tax on food, refreshment or merchandise served to Pavillion Room patrons subsequent to 10:30 p.m., if the tax were applicable. The Court gave Judgment for the Defendant in the amount of $7,463.86 which included the adjustment for the clerical error and the $5,200.63 cabaret tax after 10:30 p.m. with adjustments as shown on page 87 of the record.

Pavillion Room.

As appellant has stated, Ciro's is a famous night club located on Sunset Boulevard in Los Angeles. Three issues are involved in this proceeding: the taxability of receipts from Ciro's (1) Pavillion Room; (2) Ciroette Room, and (3) "closed house parties" which took over the entire club for the exclusive use of private organizations when Ciro's was closed to the public. The Pavillion Room is located in a separate building which was added to the Ciro establishment some years after the original structure was built. The Pavillion Room is located adjacent to the lounge and is separated from it by a movable wall and thick soundproof curtain. The floor of the Pavillion Room is slightly above that of the lounge which is between the Main Room and the Pavillion Room. The Pavillion Room was used primarily to accommodate private organizations which reserved the room for the evening for the exclusive use of their members. On occasion, however, part of the Pavillion Room was used for overflow crowds. In issue in this proceeding is the taxability of services, food and refreshments served to 304 private parties in the Pavillion Room. These parties normally commenced around 7:00 p.m. and the dinner would usually be com-

pleted before 9:30 or 10:00 p.m. On some occasions the movable wall would be moved back at 10:30 p.m. when the floor show began. Prior to this, the private organization would have paid the tab for the dinner and the waiters would have departed, leaving the dishes on the table. With respect to the dinners served in the Pavillion Room, there were some 25 basic differences between the method of operation there and that carried on in the Main Room. For example, the table set-up was different; there was no parking fee; the prices of drinks were different; the waiters served all evening until closing; the waiters worked on a different hourly basis; the menu was prearranged in the Pavillion Room, whereas service was a la carte in the Main Room; prices in the Main Room were 40% to 60% higher than in the Pavillion Room; service was different in that vegetables were served in different dishes in the Main Room but usually on the same plate in the Pavillion Room; payment was made for all tables on one check in the Pavillion Room but in the Main Room payment was made for the tables individually; and dinners were compulsory to patrons in the Pavillion Room but not in the Main Room. In order to see the floor show, patrons in the Pavillion Room would have to move up front to get a clear view. The Pavillion Room had its own separate entrance although ingress and egress was possible by way of the lounge. The rest rooms were shared in common with the Main Room although entrance could be made from the Pavillion Room itself.

Ciroette Room.

The Ciroette Room, like the Pavillion Room, was used to accommodate private parties. It is located on the second floor of Ciro's and members of the Ciroette private parties would have to go down a flight of stairs and pass

through two doorways in the Main Room in order to view the floor show. It was stipulated that 5% of the Ciroette patrons did, in fact, view the floor show so if any cabaret tax were due it would be computed on the basis of 5% of the Ciroette receipts. The same basic difference between services in the Ciroette Room and the Main Room as were mentioned with respect to the Pavillion Room, apply to the Ciroette Room.

Closed House Parties.

The Government assessed a cabaret tax on the receipts from twenty "closed house" private parties held during the period involved on the ground that engaging the whole of Ciro's by the private organization was "regarded as a mere reservation of tables." (App. Br. 33.) On these twenty nights Ciro's was closed to the public, the complete establishment having been engaged by private organizations.

Summary of Argument.

Pavillion Room.

The Trial Court correctly held that the private parties in the Pavillion Room did not constitute a public performance for profit prior to 10:30 p.m. when the folding wall was removed and therefore no cabaret tax was incurred on charges for food, refreshment and services prior to 10:30. This is in direct conformity to the holding of this Court in *La Jolla Casa de Manana v. Riddell,* 106 Fed. Supp. 132, aff'd *per curiam,* 206 F. 2d 925. It was there held that the Casa de Manana was not a cabaret from 12:00 p.m. to 2:00 a.m. after the entertainment had ceased despite the fact that post-midnight patrons had enjoyed the entertainment before midnight. The District Court could not have applied the *Casa de Manana*

case in any other way because the same basic issue was involved in the pre-entertainment period that was involved in the *Casa de Manana* post-entertainment period. Obviously, patrons of the Casa de Manana were "entitled to be present" at the entertainment because it was undisputed that some of the patrons who remained after midnight (which was the basis of the assessment) had actually been present at the entertainment. Despite the literal wording of the statute, this Court held that patrons who enjoyed the entertainment and were therefore "entitled to be present" at the entertainment were nevertheless not subject to tax because at 12:00 midnight the Casa de Manana ceased to be a cabaret. Consistently with this the Trial Court held in the instant case that private parties in the Pavillion Room prior to 10:30 p.m. did not constitute a cabaret. The District Court having decided as a fact that these private parties did not constitute a cabaret, this Court should not set aside such a finding if there is any substantial evidence to support it. (Rule 52(a), F. R. C. P.)

Ciroette Room.

The above argument applies with even greater force to the Ciroette Room which is on the second floor of Ciro's. As the District Judge stated in his Opinion ". . . the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room. . . ."

Closed House Parties.

The informal Treasury ruling set out at page 33 of Appellant's Brief is so absurd on its face that this Court should hold it to be invalid. To say that the exclusive engagement of a complete establishment such as Ciro's for a night by a private organization is to be "regarded as a mere reservation of tables" is the same as saying the

one who rents a house is merely reserving the chairs, beds, tables and other furnishings therein. In any event, the regulation itself applies only to an affair held "in a room at a hotel." Certainly Ciro's cannot be regarded as a room in a hotel. Furthermore, the District Court held as a fact that Ciro's did not furnish the entertainment and therefore the regulation by its own terms could not apply. That is, the District Court did not pass on the validity of the regulation but decided that the facts of the case did not bring Appellee within the terms of the regulation. This Court, in view of the evidence adduced, should not reverse any such finding of fact as being "clearly erroneous."

ARGUMENT.

Appellant's main thesis appears to be that the District Judge failed to give a literal meaning to the words in Section 1700(e) of the Internal Revenue Code and has used a subjective test in determining taxability. At the outset it should be emphasized that the Government itself does not interpret the words of the Code literally and this Court in the *La Jolla Casa de Manana* case[1] demonstrated the impossibility of ascribing to some of the words their ordinary meaning. The phrase "entitled to be present" is the one most responsible for the ambiguity of this section. The Treasury in its own regulations holds that this phrase does not mean what it says. In Rev. Rul. 54-487, 1954-2 Cum. Bul. 376 (Regs. 43, Sec. 101.13) it is stated:

> "It is held that payments for food, refreshment, service or merchandise, made prior to the beginning of the entertainment in a cabaret, roof garden or other similar place, are subject to the cabaret tax imposed by §1700(e) of the Code where the patrons

---

[1]106 Fed. Supp. 132, affd. *per curiam,* 206 F. 2d 925.

> or guests by or for whom such amounts are paid remain for any portion of the entertainment afforded. However, *the tax does not apply to payments made by or for patrons or guests who leave the establishment prior to the beginning of the entertainment, or who enter and leave during an intermission period, or who enter after the entertainment has ceased.*" (Emphasis supplied.)

Thus, the Commissioner by his own regulations concedes that he cannot interpret the words "entitled to be present" in the ordinary sense. That is, the test of taxability is whether or not the patron was *actually* present during the entertainment and not whether he was *entitled* to be present.

As more fully explained later herein the legislative history of Section 1700(e) shows that the Congress intended the word "entitled" to mean *presently* entitled to view the entertainment, not entitled to be present in the past or in the future. And as the District Judge said in the *Casa de Manana* case (p. 135)

> "if a patron purchased refreshments during the progress of the dancing, he could not avoid the tax by electing to leave without dancing because he was *entitled* to be present during a portion of such performance." (Italics in original.)

As further explanation the Court said:

> "It is clear that Congress evidenced *an essential unity between the service of refreshment and the enjoyment of the entertainment.* The reason for this unity is the reason for the tax itself: that the payment for the refreshment should operate to entitle the patron to view the entertainment, or participate in the dancing, as the case may be." (Emphasis supplied.)

If the word "entitled" were used in its ordinary sense, it would mean that the cabaret tax would apply to payments made for lunch even though the entertainment did not begin until 10:30 p.m. because the patron would be entitled to view the entertainment if he stayed in the establishment throughout the afternoon and evening.

As stated above, the fact that the words "entitled to be present" are to be considered in terms of the "essential unity between the service of refreshment and the enjoymnt of entertainment" is borne out by the legislative history of Section 1700(e) itself. The predecessor of Section 1700 (e) was part of a Revenue Act imposing an *admissions* tax. It was enacted in 1917 (40 stat. 318) as an emergency measure to help finance our part in World War I. The Section was amended several times but basically it has retained its identity as an admissions tax provision. The report of the House Ways and Means Committee (No. 45, 65th Cong. 1st Sess. p. 8) states that a tax is being levied equivalent to 10% of the "amount paid for admission to any place to which admission is charged." The tax was applied to admissions to theatres, circuses, cabarets, ball games and similar entertainments. Administrative difficulties were encountered in applying the tax to cabarets because admission charges were generally not made and the tax was basically an admissions tax. Under Treasury Rulings a breakdown of charges was made so as to ascertain what portion could be attributed to the admission price. Then in 1919 the Act was amended to incorporate various rulings of the Treasury Department. The Act, as amended, continued to impose an admissions tax. In order to apply the tax to cabarets under the Code provision imposing the admissions tax, the Treasury computed the tax on the *difference* between the regular price for refreshments and the cabaret price; for example, if

the bar price of a drink was 15¢ (remember, this is 1917) and the cabaret price was 50¢, the tax would apply to the difference of 35¢ on the theory that this was the "admission" charge. (See hearings on H. R. 4280, Revenue Bill of 1917 quoted in *Gear v. Birmingham,* 88 Fed. Supp. 189 at 196.) Accordingly, if there was an increase in price during the public performance, the tax would apply to the increase. The original Act as amended, became part of the Internal Revenue Code of 1939 as Section 1700(e). Because of the difficulty of its administration, the section was amended in 1949 so that a 5% tax was imposed on the *total charges.* However, it did not change the base on which the tax was applied which was on sales made during the period there was a *public performance for profit.* The tax was increased to 20% in 1944.

It is clear from the legislative history that the cabaret tax was intended by Congress to apply to purchases of food and beverage only "while the floor show is in progress." See for example, the statement in the Senate Report accompanying the Revenue Act of 1942 (77th Cong., 2nd Sess., Report 1683, p. 79):

> ". . . In order to allay possible questions under the present statute, the amendment specifies that the tax, levied on *amounts paid by or for any patron or guest entitled to be present during any portion of the performance shall be applicable,* although no increase is made in the charges for admission, refreshment, service, or merchandise by reason of the furnishing of the performance. Thus the tax will be collected although a cabaret does not increase its prices for food or beverages *while its floor show is in progress.* The amendment confirms the Treasury Department's interpretation of the present statute by stating that the tax is applicable in the case of any room in any

hotel, restaurant, hall, or other public place *where music and dancing privileges or any other entertainment,* except instrumental or mechanical music alone, *are afforded the patrons in connection with* the serving or selling of food, refreshment or merchandise." (Emphasis supplied.)

Should any doubt remain as to the Congressional intent, it ought to be dispelled by a reading of the Committee Report accompanying H. R. 17 which passed the House in May, 1957 but not the Senate. In the accompanying H. R. 869 it is stated,

". . . in the case of the cabaret tax, the 20% rate is particularly onerous because, although this tax is classified as an admissions tax, its base includes not only the price paid for any admissions, but also the amounts paid for refreshments, services, and merchandise. *Moreover, the 20% rate applies only where there is a combination of entertainment and the service of food or beverages.* Where only entertainment is provided the 10% admissions tax usually applies; on the other hand, where there is only the serving of food and beverage, generally no tax is imposed. Thus the 20% tax discriminates against the combination of food and beverages or entertainment, *since either, if provided separately, is taxed at a lesser rate or is not taxed at all."*[2] (Emphasis supplied.)

---

[2]It is interesting to observe that the House, in its Report further noted: "In addition, testimony before a Sub-Committee of your Committee, has indicated that this discriminating high rate of the cabaret tax has had a serious adverse effect on the employment of musicians and other entertainers." (1957 P-H 44,958 Para. 33,005). This observation was undoubtedly based on a study which was reported in Federal Tax Policy for Economic Growth and Stability,

Appellant complains in its Brief that the District Court in refusing to read the Code section literally, concluded that: "A literal translation of the above provision would ascribe to Congressional intent a most arbitrary and unreasonable basis on which the tax is imposed." (App. Br. 18.) As previously pointed out, the Treasury, by its own regulations, has refused to give the words "entitled to be present" a literal meaning. (Rev. Rul. 54-487.)

Appellant in its Brief (p. 19) sets out the issue in these words,

> "Consequently it is our position that it was the intention of Congress to impose a cabaret tax on all amounts paid for food, refreshment, service or merchandise by or for patrons or guests who are entitled to be present during any part of the public performance given at a cabaret for profit."

Joint Committee on the Economic Report published by the United States Government Printing Office, Washington, D. C. It was there stated:

> "A pilot study in five cities, Boston, Detroit, Denver, Minneapolis, and Memphis, was financed by the American Federation of Musicians. On the basis of this study, it was believed by the research agencies that a more extensive survey would support the conclusions:
>
> 1. That establishments subject to this 20 percent cabaret tax are more important sources of employment for musicians, and that job loss in these establishments since 1943 had been much heavier than has been recognized;
>
> 2. That elimination of the 20 percent cabaret tax would lead to a very substantial increase in employment of musicians, entertainers, waiters, waitresses, and other service and kitchen help; and
>
> 3. That loss of tax revenue to the Treasury through elimination of this tax would be offset by increased income-tax payments."

Compare this with the following statement made in the Government Brief filed with this Court in the *Casa de Manana* case (p. 9):

> "It is the Collector's position that taxpayer's establishment was at all times a 'cabaret or other similar place' and that the tax imposed under §1700(e) applied to 'all' refreshments purchased by any patron present during any portion of the entertainment at taxpayer's establishment.
>
> "Section 1700(e) does not require that the consumption of the refreshment be simultaneous with the entertainment but rather contemplates the taxation of any amounts paid throughout the evening by one who is present during the entertainment. This is clear from the use of the language *'all* amounts paid for . . . refreshment.'"

This argument was completely rejected by this Court in the *Casa de Manana* case and the result of the decision was nullification of a Treasury regulation similar to the one invoked in the instant case. There an attempt was made to interpret Section 1700(e) as applying to charges made at the Casa de Manana between 12 midnight and 2:00 a.m. The *Casa de Manana* principle must apply here because the private parties in the Pavillion Room did not constitute a cabaret prior to 10:30 p.m. In other words, what is concededly a private group having a dinner meeting is simply not a cabaret and in attempting to invoke what he considers an applicable ruling, the Commissioner is doing nothing more than what he unsuccessfully attempted to do in the *La Jolla de Manana* case.

So, it is quite obvious that the instant case is but another example of an effort to effect administrative legislation. In at least two recent attempts in this District to

enlarge the operation of Section 1700(e)(1) the Government has met with defeat. An unsuccessful effort to stretch the Code to cover a similar situation is found in *Naylor v. United States,* 102 Fed. Supp. 309. District Judge Ben Harrison was not impressed with Defendant's argument that income from "public" dances held in the private Beverly Hills Club was subject to cabaret tax.

As previously demonstrated, in *La Jolla Casa de Manana v. Riddell,* 106 Fed. Supp. 132 (aff'd, *per cur.,* 206 F. 2d 925) the Government unsuccessfully took a position directly parallel to the one adopted in this case. Despite the fact that the law was made clear in this Circuit in the above 1953 decision as to when a cabaret was a cabaret and when it was not, the Commissioner in 1954 issued a contrary ruling (Rev. Rul. 54-487 C. B. 1954-2, p. 376). Judge Byrne decided that the cabaret tax could not be imposed except during the hours when the establishment was operating as a cabaret. The Commissioner completely ignores this in the above ruling, saying "for the tax to apply, it is not necessary that such patrons or guests be able to witness the entertainment and partake of food or refreshment at the same time."

At this juncture we might point to some of the similarities between the *La Jolla* and *Ciro* cases:

La Jolla Casa de Manana.	*Ciro.*
1. "Some of the patrons to whom refreshment was sold between 12:00 midnight and 2:00 a.m. had been present during part of the entertainment period prior to midnight." (Opin. p. 133.)	1. Some of the patrons in the private parties in the Pavillion Room had been present during part of the entertainment after 10:30 p.m. [R. 72.]

2. "Plaintiff never had, and does not now have, any records showing separately the amount of refreshments sold to each class of patrons." (P. 133.)	2. Plaintiff never had and does not now have any records showing separately the amount of refreshments sold to each class of patrons. [R. 70-71.]
3. The Commissioner proposed an assessment of cabaret tax on all receipts from 12:00 midnight to 2:00 a.m. (P. 133.)	3. The Commissioner assessed cabaret tax receipts prior to entertainment time, 10:30 p.m., as well as during entertainment. [R. 71-72.]
4. After protest by Plaintiff the Commissioner ruled that only one-third of such assessment would be made on the theory that one-third of the receipts represented the portion received from patrons who had been present during some portion of the music and dancing between 9:00 p.m. and 12:00 midnight. (P. 133.)	4. The Commissioner ruled that since 94% of sales in the Main Room were taxable, 94% of sales in the Pavillion Room were taxable on the theory 94% of the patrons in the Pavillion Room private parties stayed to view the entertainment. [R. 71-72.]
5. The Government argued that since the patrons were present at the dancing *before* 12:00 p.m. they could be taxed on sales made after 12:00 p.m. (P. 134.)	5. The Government argues that since Pavillion Room patrons were present during the floor show, sales made *prior* to 10:30 p.m. can be taxed. [R. 49.]

It may be pertinent to note here that the Commissioner of Internal Revenue follows the practice of entering an "acquiesence" or "non-acquiesence" when a decision of the Tax Court of the United States is against him. It is

his practice also to follow or refuse to follow other Court decisions (except those of the Supreme Court of the United States). This procedure is justified on what is asserted to be an interest in the uniform application of the tax laws. In the instant case the Internal Revenue Agents who set up the tax deficiency followed the Commissioner's instructions which are supposed to be uniformly applied in all districts of the United States. The agents neither had the duty to nor apparently did they consider the applicability of certain judicial decisions promulgated in this judicial district and circuit.

Were it not for the rather unique position which the Commissioner of Internal Revenue maintains, the conflict between the decision of this Court in the *Casa de Manana* case and the regulations applied in the case at bar would not be stressed herein. The Tax Court of the United States has in the past, taken the position that it need not follow a Court of Appeals decision in the Circuit in which it is trying a case. But it goes without saying that the District Court for the Southern District of California should follow a decision of the Court of Appeals for the Ninth Circuit whether or not such a decision is contrary to a ruling of the Commissioner of Internal Revenue.

This Court was not in agreement with the Commissioner prior to the *Casa de Manana* decision as to what the following meant:

> "public performance for profit"
>
> "entitled to be present during any portion of such performance"
>
> "where dancing privileges or any other entertainment * * * are afforded the patrons in connection with the serving or selling of food, refreshment or merchandise"
>
> "cabaret"

And, as we have pointed out above, the Commissioner was still in disagreement after the *Casa de Manana* case was decided. In determining what cabaret tax should be imposed on Ciro's he used his own definitions.

Here it might be appropriate to quote from one of the classics.

> "I don't know what you mean by 'glory,' " Alice said.
> "Humpty Dumpty smiled contemptuously. "Of course you don't—till I tell you. I meant 'there's a nice knock-down argument,' " Alice objected.
> "When I use a word," Humpty Dumpty said in rather a scornful tone, "it means just what I choose it to mean—neither more nor less."
> "The question is," said Alice, "whether you *can* make words mean so many different things."
> "The question is," said Humpty Dumpty, "which is to be master—that's all."
> Lewis Carroll's "Through the Looking Glass" Illustrated Editions Company, page 188.

So, even though the Commissioner "*can* make words mean so many different things," the District Court has a right to assume that the Court of Appeals is "master," not the Commissioner.

Attention should be called to a manifest error in Appellant's Brief at page 25. It is stated as follows:

> "Obviously in the La Jolla case, amounts spent from midnight to 2:00 a.m. could not entitle any patron to be present at the dancing or to hear the music which had ceased at midnight and *for that reason* it was held that no tax could be imposed on such. amounts." (Emphasis supplied.)

In the Opinion in the *La Jolla* case (106 Fed. Supp. 132-133) we find the following:

> "On June 28, 1949, the Commissioner of Internal Revenue proposed a deficiency in cabaret tax against plaintiff amounting to $947.10, covering the periods from July to October of 1947, July to September of 1948, and January to April of 1949, based on the total refreshment receipts during such period from midnight to 2:00 o'clock A.M. Plaintiff protested such proposed assessment in writing; thereafter, the Commissioner ruled that only one-third of such proposed deficiency should be assessed against plaintiff, on the theory that approximately one-third of the total receipts represented the portion received from patrons *who had been present during some portion of the music and dancing between 9:00 o'clock P.M. and midnight.* Plaintiff paid the tax and filed a claim for refund, a claim which was rejected. This litigation has resulted." (Italics in original.)

The Court, of necessity, in deciding for the taxpayer determined that the cabaret tax could not be applied on sales to patrons "who had been present during some portion of the music and dancing between 9:00 p.m. and midnight." So, clearly, the reason for the decision in the *La Jolla* case was not that post-midnight patrons were not entitled to be present at the dancing or to hear the music. If the patrons were there, certainly they must have been entitled to be there. In other words, the Court decided in the *La Jolla Casa de Manana* case that the establishment was not a cabaret between 12:00 midnight and 2:00 a.m. therefore sales made during those two hours were not taxable even though the patrons had previously enjoyed the entertainment. In the instant case the Court decided that the private parties in the Pavillion

Room from 7:00 p.m. to 10:30 p.m. were not a cabaret and that sales during these hours were not taxable. It is difficult to see how the District Court could have decided otherwise without being inconsistent with the *Casa de Manana* case.

The Government asserts in its brief that the District Court applied a "subjective test" in arriving at its decision. (App. Br. 23.) Actually, the judge did the same thing that Judge Byrne did in the *Casa de Manana* case. He determined that these private parties did not constitute a cabaret during certain hours (7:00 p.m. to 10:30 p. m.). There is nothing subjective about such a factual determination. Indeed, the judge was careful to limit the applicability of his decision by admonishing:

> "I do not mean to suggest that the Treasury Regulations taxing such receipts should be denied any meaning and effect. Certainly, to allow pre-performance receipts in each and every case to escape the imposition of a tax would serve to provide a facile means for tax avoidance, would compound the already existing difficulties present in tax collection and administration, and would be as much productive of inequities and as lacking in logic as would be the adoption of the other extreme—holding all pre-performance payments by persons remaining for the public performance within the pale of this statute. The only sensible and practical approach to the problem is to *consider the wording of the statute in the light of each factual situation* as it is presented keeping always in mind the objectives and purposes the statute sought to achieve." (Emphasis supplied.) [R. 51-52.]

The Court's holding that the private party activities prior to 10:30 p.m. did not constitute a cabaret is entirely

consistent with the evidence. The public was not admitted and there could not have been a "public performance for profit." It must be conceded that if the entertainers had been brought into the Pavillion Room and the performance had there taken place, the tax would not apply because the mere performance or entertainment does not make what would otherwise be a private performance, a public performance for profit. In making the assessment the Commissioner lost sight of the fact that it is the admittance of the public without restriction that makes for taxability—not that there is entertainment. (*McKenzie v. Maloney,* 71 Fed. Supp. 691; *Daum v. Jarecki,* 123 Fed. Supp. 583; *Southland Club v. Broderick,* 1956 P-H 44,578; *United States v. Lambeth,* 176 F. 2d 810 (C. C. A. 9).)

The interpretation of Section 1700(e) by the District Court is manifestly correct in the light of its legislative history and prior judicial decisions construing it. Accordingly, in reviewing this decision it is suggested that the following rule with respect to tax provisions, enunciated in another tax case, should be applied:

> "It is the established rule not to extend their provisions, by implication, beyond the clear import of the language used, or to enlarge their operations so as to embrace matters not specifically pointed out. In case of doubt they are construed most strongly against the government, and in favor of the citizen." (*Gould v. Gould,* 245 U. S. 151.)

Even assuming, in Appellant's words, that the District Court's test "would be difficult to make and is not a satisfactory one in the exact field of taxation" (App. Br. 23) it is not clear, as indicated in the fn. 2, pp. 10-11, *supra;* whether exclusion of such private parties from cabaret tax would have an over-all adverse tax effect from the Govern-

ment standpoint. In any event, if a change in tax policy is to be made, it is for the Congress to make it.

> " 'If in practice' these sections are causing 'such loss of revenue as to indicate that Congress may have erred in its balancing of the competing considerations involved, the amendment must obviously be enacted by the Congress and not the Commissioner of Internal Revenue or this Court.' " (*Commissioner v. Korell,* 339 U. S. 619, 626 (1950).)

As will be urged in connection with the two remaining issues, herein, the familiar Rule 52(a), F. R. C. P.[3] should control with respect to the trial court's findings of fact regarding the Pavillion Room. The Trial Judge viewed the premises and heard the witnesses. There was, indeed, substantial evidence to support all his findings.

The Ciroette Room.

The Court viewed Ciro's premises in the presence of Counsel for both parties. The Ciroette Room was found to be located on the second floor of Ciro's. The Main (entertainment) Room could be entered by Ciroette private party patrons only after they had descended fourteen steps, cross a breezeway, and passed through two doorways. The Government assessed cabaret tax on 5% of the receipts from private parties held in the Ciroette Room on the ground that 5% of the private party patrons went downstairs to see the floor show after 10:30 p.m. The Trial Court concluded that

> "the nature of these private parties being similar to those conducted in the Pavillion Room my prior

---

[3]Rule 52(a) of the Federal Rules of Civil Procedure provides, in part, as follows:

> "Findings of Fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses."

discussion on this subject is pertinent here and does not have to be repeated; however, the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room and the subsequent effort and distance to be traversed for its patrons to observe the floor show. I find therefore, that the tax assessment on the 5% of the Ciroette Room's receipts is improper."

It should be made clear that the assessment of the cabaret tax was on pre-performance receipts from private party patrons in the Ciroette Room. Any purchases in the Main Room after show time by patrons who had come downstairs from the Ciroette Room were taxed at 20% and there is no dispute in this case about the taxability of such post-entertainment charges.

The prior discussion concerning the Pavillion Room, is applicable to the Ciroette private parties and will not be repeated here. It seems appropriate however, to urge that this Court again apply Rule 52(a) (F. R. C. P.) and sustain the Trial Court on the ground that its findings are amply supported by the evidence. Even if this Court should take a different view of the facts it seems evident that there is sufficient evidence in support of the Trial Court's decision so that under Rule 52(a) the decision should be affirmed. As Judge Johnson said in *Nee v. Linwood Securities Co.,* 174 F. 2d 434, 437 (C. A. 8) in sustaining the Trial Court:

"That the trial court could have viewed the facts differently, or that we might perhaps have done so, if we had been the initial trier thereof, does not alone entitle us to reverse. Under Rule 52(a) and its interpretation in the United States Gypsum Co. case, there must exist a stronger basis for over-throwing

a finding of fact than a mere difference in personal judgment. Such evidentiary weight and such convictional certainty must be present that the appellate court does not feel able to escape the view that the trial court has failed to make a sound survey of or to accord the proper effect to all the cogent facts, giving due regard, of course, to the trial court's appraisal of witness credibility where that factor is involved."

Private Parties (Closed House Parties).

On 20 different evenings, usually on Sunday, private organizations held affairs in Ciro's which was then closed to the public. The Government imposed the cabaret tax on the basis of a recent ruling which reads as follows [R. 61]:

"Where a private organization arranges to hold an affair in a room at a hotel which normally is operated as a cabaret and the affair is held under such circumstances that *the hotel furnishes practically the same services, including entertainment,* during the same hours that the room is operated as a cabaret, *the arrangements made by the private organization are regarded as a mere reservation of tables.* In such case, the Bureau holds that the room is operated as a cabaret on such occasions, even though the patronage is limited to the members, together with the guests of the private organization, and the private organization furnishes entertainment in addition to that furnished by the hotel * * *

"Where a private organization holds a dinner in a room at a hotel, under such circumstances that the hotel does not furnish any entertainment but the private organization does provide dancing facilities for the persons (120) attending by hiring an orchestra,

> or furnishes other entertainment, cabaret tax does not apply to any amount paid in connection with the affair." Special Ruling, August 31, 1949, 5 CCH 1950 Stand. Fed. Tax Rep. Para. 6053. (Emphasis supplied.)

The Ruling has not been passed upon by any Court, however, there are cases dealing with the question of what constitutes a "public performance for profit." (See *United States v. Lambeth,* 176 F. 2d 810 (C. A. 9, 1949); *Naylor v. United States,* 102 Fed. Supp. 309 (S. D. Cal. 1952); *Bomber Club v. Broderick,* U. S. D. C. Kan. 223, 54 Para. 72,685 P-H 1954.)

In reaching out to make this assessment the Commissioner indulged in the fantastic presumption that where a private organization holds an affair in a place which is normally operated as a cabaret, it is subject to cabaret tax on the ground that "the arrangements made by the private organizations are regarded as a mere reservation of tables." This is quite the same as saying that a lessee who rents a furnished apartment obtains from the lessor only a reservation of furniture in the apartment. It should be noted that the Ruling, absurd as it is, applies only "where a private organization arranges to hold an affair in a room at a hotel." Certainly Ciro's is not a room in a hotel.

Not only does the Ruling appear to be invalid but it was improperly applied in this case. Be that as it may, we need not pass on the issue because the District Court found as a fact that "the evidence conclusively establishes that the private organizations themselves contracted for the entertainment and the music." [Opin. R. 62.] The Court was justified in making such a finding on the basis of the testimony. The plaintiff, for example, testified that

in most of the cases the Closed House parties provided their own entertainment and music. Also, they might take only part of the regular Ciro's show and supplement it with their own acts. [R. 201 *et seq.*] As the plaintiff testified, "every party is on its own and we had no control over the show or the party." [R. 206.] Payment was made directly to the entertainers and musicians by the private party. So, by its own terms the ruling cannot apply because Ciro's did not "furnish . . . entertainment."

It is difficult to see how the Court could have decided otherwise. However, even if this Court should interpret the evidence differently, the findings of fact, being supported by substantial evidence, should not be set aside as being "clearly erroneous."

As the Supreme Court said in *United States v. U. S. Gypsum Co.,* 333 U. S. 364, 68 S. Ct. 528

> "Since judicial review of findings of trial courts does not have the statutory or constitutional limitations of findings by administrative agencies or by a jury, this court may reverse findings of fact by a trial court where 'clearly erroneous.' The practice in equity prior to the present Rules of Civil Procedure was that the findings of the trial court, when dependent upon oral testimony where the candor and credibility of the witnesses would best be judged, had great weight with the Appellate Court."

In *United States v. Yellow Cab Company,* 338 U. S. 338, 70 S. Ct. 177 (1949), Mr. Justice Jackson speaking for the Court said:

> "It ought to be unnecessary to say that Rule 52 applies to appeals by the Government as well as to those by other litigants. There is no exception which permits it, even in an antitrust case, to come to this

> Court for what virtually amounts to a trial *de novo* on the record of such findings as intent, motive and design. While, of course, it would be our duty to correct clear error, even in findings of fact, the Government has failed to establish any greater grievance here than it might have in any case where the evidence would support a conclusion either way but where the trial court has decided it to weigh more heavily for the defendants. Such a choice between two permissible views of the weight of evidence is not 'clearly erroneous.' "

Judge Sanborn of the Court of Appeals for the Eighth Circuit, said in *Cleo Syrup Corp. v. Coca-Cola Co.,* 139 F. 2d 416:

> "This Court, upon review, will not retry issues of fact or substitute its judgment with respect to such issues for that of the trial court. (citing cases) The power of a trial court to decide doubtful issues of fact is not limited to deciding them correctly. (citing cases) In a non-jury case, this Court may not set aside a finding of fact of a trial court unless there is no substantial evidence to sustain it, unless it is against the clear weight of the evidence, or unless it was induced by an erroneous view of the law." (Citing cases.)

The Supreme Court in *McCaughn v. Real Estate Land Title and Trust Co.,* 297 U. S. 606, reversed a decision of the Court of Appeals which had reversed a judgment of the District Court, rendered in a tax case prior to the adoption of Rule 52. There the District Court trying the case without a jury held that a certain transfer had been made in contemplation of death. The Court of Appeals on review, decided that the transfer was not made in con-

templation of death and reversed the judgment. In reversing the Court of Appeals, the Supreme Court said:

> "the instant case is controlled by the established rules relating to appellate review in actions at law where a jury trial has been waived . . . where a general verdict is found by the trial court, it has the same effect as the verdict of a jury. The Appellate Court cannot pass upon the weight of evidence (citations)" . . . "The ultimate question for the decision of the trial court was one of fact and its general verdict was conclusive. The Circuit Court of Appeals was without authority to weigh the evidence and to make its own findings."

Rule 52(a) and the general rule as enunciated by the Supreme Court was followed by this Court in a recent tax case (*United States v. Lambeth,* 176 F. 2d 810) involving the identical section here under consideration. *i. e.* Section 1700(e). This Court through Judge Bone there remarked:

> "On this record we think that the case falls within Rule 52(a) of the Federal Rules of Civil Procedure, 28 U. S. C. A., in part providing: 'Findings of fact shall not be set aside unless clearly erroneous, * * *.' Clear error calling for reversal is not present and the Government's presentation fails to convince us otherwise. Affirmed." (*Wittmayer v. United States* (9 Cir. 1941), 118 F. 2d 808, 811.)

In the *Lambeth* case the taxpayer claimed to be operating a private club; however, taxpayer did not have a club license under Oregon law. In fact taxpayer's license "contemplated services to the general public." This Court in its opinion noted that " 'admittance' cards were apparently accessible to anyone who decided to 'join'." Never-

theless, even with such a "liberal guest policy" it was held that the taxpayer was not "serving the public and was thus not furnishing a public performance for profit within the definition of the Federal taxing statute." (See also *McKenzie v. Maloney,* 71 Fed. Supp. 691; and *Southland Club v. Broderick,* 1956 P-H 44,578; *cf. Sir Francis Drake v. United States,* 75 Fed. Supp. 668 (N. D. Cal.), decided on a 1941 assessment.)

Despite the decision of this Court in the *Lambeth* case the Commissioner maintains that a private party held at Ciro's when it was closed to the public constitutes "a public performance for profit."

Certainly, the findings of fact of the trial judge adverse to the Commissioner on this issue are not "clearly erroneous."

Conclusion.

For the foregoing reasons the decision appealed from should be affirmed.

Respectfully submitted,

ERNEST R. MORTENSON,

Attorney for Appellee.